HARBOR VIEWS

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HARBOR ADVISORY

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A LOOK INSIDE HARBOR VIEWS

- *Thoughts on the Economy* – Slow or negative supply growth in oil, gas and some metals markets will help balance supply and demand over the next 18 months.
- *Our View of the Financial Markets* – European share prices should outpace those in the U.S.

LATEST NEWS FROM HARBOR ADVISORY

- You can visit us at: www.harboradvisory.com. Take a look and let us know your feedback.
- Jack De Gan continues to make news with his regular guest appearances on CNBC's top rated financial shows "Squawk Box", "The Call", "Closing Bell" and on Bloomberg TV, Fox Business News and National Public Radio.

THOUGHTS ON THE ECONOMY

The U.S. economy finished 2015 with 4th quarter GDP growth of 0.7% and the full year at 2.4%. The rate of GDP expansion since the end of the recession remains just north of 2% real growth.

The equity and debt markets continue to signal a slowdown in growth in the U.S. and more significantly in economies outside the U.S. Resource based economies such as Russia, Brazil, Australia and the oil exporting nations are softening from oil prices of $30 per barrel. Commodity price weakness in general is being interpreted by markets as weakness in demand, and therefore, slowing growth. We see it as more of an oversupply issue. The dramatic 'super cycle' in commodity prices (over the ten years from 2005-2015) engendered massive investment in commodity production and a large supply increase. Capital investment by the industry has been halved in the last 18 months which will slow or reverse supply growth in oil, gas and some metals markets. This will help balance supply and demand over the next 18 months.

Employment trends remain strong with job creation in 2015 of over 2.5 million and real wage increases of 2.5% year over year. We expect job creation to slow this year to a rate of 1.5 to 2 million new jobs but with greater wage gains. This increase, along with the huge energy dividend, will drive consumer spending growth of 2.5-3% in 2016 allowing GDP growth to approach 2.5%.

The strong dollar has been a headwind for exports over the last 18 months as the trade-weighted dollar increased in value by about 20%. This strength will moderate but our exports will show little growth this year.

HARBOR ADVISORY

WWW.HARBORADVISORY.COM

Phone:
603-431-5740

Fax:
603-431-2927

500 Market Street,
Suite 11,
P.O Box 4520
Portsmouth, NH
03802-4520

harboradvisory.com

Harbor Views is written and produced by Harbor Advisory.

Jack De Gan
Editor

Weld Butler

Jan Yeaman

Cheryl Crowley

OUR VIEW OF THE FINANCIAL MARKETS

Equity markets were disappointing in 2015 in the U.S. and worldwide. In the U.S. the S&P 500 produced a total return of 1.4% while the broader MSCI-All Country World Index declined by 2.4%. Within those figures the strength was narrowly focused on a few highfliers. Most issues fell. The strength of the dollar accounted for much of the earnings shortfall while lower oil and metals prices crushed earnings in corresponding industries. We think that pig has moved through the python and will provide much less of a headwind in 2016.

Corporate earnings could grow by 4-6% this year with equivalent equity price rise plus the dividend return. The growth scare that caused the sharp correction in January and February will pass as it becomes clear the U.S. economy is resilient and that China's economy is growing more slowly, but not collapsing.

European share prices should outpace those in the U.S. as unusually low valuations on the continent should begin to 'revert to the mean'. We think the same can happen in the emerging markets although the timing of that reversion may require a bit more patience.

Bond yields continue to confound the consensus as the 10 year Treasury, which finished 2015 essentially unchanged at 2.15%, has decreased to 1.73% at this writing.

The Federal Reserve increased interest rates for the first time in nine years in December moving the Federal Funds target up by .25%. There may be one or two more rate increases of the same size in store for 2016.

Some are concerned that the negative interest rate policy (NIRP) being pursued in a number of European countries and in Japan indicates the risk of deflation and recession ahead. We do not see that in the U.S. We expect inflation in the U.S. to continue to rise slowly at the core rate of 1.5-2% this year. If we are correct, the yield on the 10 year Treasury could rise back to the 2-2.5% area by year's end.

TAX SEASON FRAUD

The wonders of the internet age are many. Unfortunately, they are accompanied by risks of fraud. The IRS has renewed a consumer alert for trick emails designed to fool taxpayers into thinking they are official IRS emails. **DO NOT** click on links in suspect emails which connect to fraud sites requesting personal information or that can infect a computer with a virus. Forward the email directly to phishing@irs.gov for corroboration of authenticity.

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